Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Wayne	Analyst:	Jeff Garnier	Bill Number:	ABX 102
Related Bills:	See Legislative History	Telephone:	845-5322	Introduced Date:	March 1, 2001
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Energy Efficient Heating and Cooling System Credit

SUMMARY

This bill would provide individuals a credit of 25% of the cost of an energy efficient heating and/or cooling system installed in an individual's home.

PURPOSE OF THE BILL

The purpose of the bill is to provide a tax incentive, in addition to lower energy utility bills, for purchasing and installing energy efficient heating and/or cooling systems.

EFFECTIVE/OPERATIVE DATE

This credit would be effective immediately and operative for taxable years beginning on or after January 1, 2001, and before January 1, 2006.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Federal law currently provides two energy-related credits: an energy investment credit, and a business credit for the production of electricity.

The energy investment credit is equal to 10% of the basis of energy property placed in service during the taxable year. Energy property includes equipment that uses solar energy to generate electricity, to heat or cool a structure, or to provide solar process heat. It also includes equipment that produces, distributes, or uses energy derived from geothermal deposits. The equipment also must meet performance and quality standards prescribed by federal regulations.

The business credit is for the production of electricity from certain renewable resources.

Board Position:			Department Director	Date
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Prior federal law allowed a credit equal to 15%, up to a maximum total credit of $300, for the purchase and installation of energy-saving components in an individual's residence. The qualifying expenditures included such items as:

- energy efficient furnace burners and electrical or mechanical furnace ignition systems; and
- storm or thermal windows or doors, and caulking or weather-stripping of exterior doors or windows.

Prior state law allowed a credit equal to a percentage of the cost of energy conservation measures. The credit was changed a number of times during its lifetime and was available for tax years 1977-1986. In later years, the credit for residential property was 40% of allowable costs for tax years 1981-1983 and 35% for tax years 1984-86. Energy measures that qualified for the credit were similar to those that qualified for the federal credit.

If the federal credit was allowed on the same costs, the state credit was reduced by the amount of the federal credit. For residential properties, the combined federal and state credits could not exceed 40% of cost. For nonresidential properties, the combined federal and state credits could not exceed 40% of cost except where the cost exceeded $6,000. In this case, the federal credit was limited to 25% of costs, and the state credit was reduced by the amount of the federal credit. The state credit was limited to a maximum of $1,500. In addition, the state credit could not be claimed if the amount of state credit for any given year would have been less than $10.

Current state law does not provide a credit for energy conservation measures.

<u>THIS BILL</u>

This bill would provide individuals a credit of 25% of the cost of a heating and/or cooling system (hereinafter system) installed in the individual's principal residence. The system must be certified by the California Energy Resource Conservation and Development Commission (CERCDC) as being energy efficient.

The bill would require the CERCDC to determine which residential systems use significantly less energy than other comparable systems. The CERCDC would certify to the Franchise Tax Board systems that are energy efficient.

<u>IMPLEMENTATION CONSIDERATIONS</u>

The bill does contain a sunset date for the credit. However, the department would be required to retain the carryover on the tax forms indefinitely because an unlimited credit carryover would be allowed. Recent credits have been enacted with a carryover limit since experience shows credits are typically used within eight years of being earned.

Any excess credit could be carried over to succeeding years until exhausted.

LEGISLATIVE HISTORY

ABX 79 and AB 872(Nakano, 2001/2002) would allow a solar energy credit. Both bills are at the Assembly Desk.

SBX 71 and SBXX 71 (Perata, 2001/2002), and ABX 27 and AB 1124 (Koretz, 2001/2002) would allow multiple credits and an accelerated depreciation deduction for the purchase of a power generation system. SBX 71 died upon the close of the first special session while SBXX 71 is at the Senate Desk. ABX 27 died upon the close of the first special session while AB 1124 is at the Assembly Desk.

ABX 15 (Rod Pacheco, 2001/2002) would allow a 100% credit for the purchase of energy conservation measures that reduce a taxpayer's electricity and natural gas use by 5% from the previous taxable year and is in Assembly Revenue and Taxation Committee.

ABX 86 and AB 1264 (Campbell, 2001/2002) would allow a 75% credit for the purchase and installation of a solar energy system for residential purposes. Both of these bills are at the Assembly Desk.

AB 873 (Takasugi, 1997/1998) would have allowed a credit equal to 40% of the cost of energy conservation measures. The bill also would have allowed a second credit equal to 10% of the cost of a solar energy system installed on premises located in California and used for commercial purposes, subject to certain requirements. The bill failed to pass the Assembly Revenue and Taxation Committee.

OTHER STATES' INFORMATION

Florida and *Illinois*: Do not have any credits based on energy conservation.

Massachusetts: Currently has an energy credit that is equal to 15% of the net expenditures or $1,000, whichever is less.

Michigan: Does not allow an energy-related credit, but exempts the value of energy conservation devices from the local property tax.

New York: For personal income taxpayers only, New York allows a credit for solar generating equipment equal to 25% of certain solar generating expenditures. The credit is capped at $3,700 per system.

The laws of these states were reviewed because their tax laws are similar to California's income tax laws.

FISCAL IMPACT

If the implementation consideration addressed in this analysis is resolved, the department's costs are expected to be minor.

ECONOMIC IMPACT

As currently drafted, this bill would result in potentially very significant revenue losses on the order of $300 million annually beginning in 2001-02.

The revenue impact of this bill would be determined by the amount of costs incurred by taxpayers for purchasing and installing energy efficient heating and/or cooling systems in their principal residences and the amount of credits that could be applied to reduce tax liabilities.

There are roughly 4.8 million owner-occupied residential housing units in California. These housing units are either detached single family, attached up to a four-plex, condominium, or mobile home.

Costs of energy efficient heating and/or cooling systems (assumes a Seasonal Energy Ratio of 12 or higher) vary depending on the size and type of housing unit. For an average size single-family detached structure, costs could range from $6,000 to $9,000. For attached structures up to a four-plex and including condominiums, costs could range from $3,500 to $7,000. For mobile homes, costs are typically in the $2,200 to $3,500 range.

In any given year, if 5% of taxpayers owning and occupying these structures were to install heating and/or cooling systems with a certified energy-efficient system at an average cost per system of $5,000, credits generated would be $300 million annually.

ARGUMENTS/POLICY CONCERNS

The credit would be allowed for the purchase of a system and installed on a personal residence located either inside or outside California.

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